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ABSTRACT

In school year 1996-97, the Department of Agriculture instituted more stringent requirements for the nutritional content of school meals. The General Accounting Office was asked to study school food-service revenues and expenses and how they had changed since the requirements went into effect. This report contains information of the sources of revenues available for providing meals, the expenses of producing meals, the revenues compared with expenses, and the approaches that local school food authorities had adopted to manage their school food-service finances. It uses data from six selected states. The study found that revenue from federal reimbursements and the sale of food were the principal sources of revenue for school food services in the 6 states reviewed for school years 1996-97 through 2000-01. Labor and food purchases were the principal expenses for the six states, sharing nearly equal proportions and changing only slightly. The 6 states had a small though increasing shortfall in total revenue compared with expenses over the 5-year period. To limit their expenses and maximize their revenues, local school food-authority officials reported buying food in bulk, hiring more part-time staff, expanding a la carte food sales and catering programs, and other strategies. (Author/WFA)

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United States General Accounting Office

GAO

Report to Congressional Requesters

May 2003

ED 477 877

SCHOOL MEAL PROGRAMS

Revenue and Expense Information from Selected States

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Highlights

Highlights of GAO-03-569, a report to Congressional Requesters

SCHOOL MEAL PROGRAMS

Revenue and Expense Information from Selected States

Why GAO Did This Study

The National School Lunch and Breakfast Programs provide millions of children with low-cost or free nutritious meals each school day. In school year 1996-97, the Department of Agriculture instituted more stringent requirements for the nutritional content of school meals. GAO was asked to study the school food service revenues and expenses and how they have changed since the requirements went into effect. This report includes information on the sources of revenues available for providing meals, the expenses of producing meals, the revenues compared to expenses, and the approaches that local school food authorities have adopted to manage their school food service finances. It uses data from six selected states. This report does not provide specific information on the expense of producing a reimbursable school lunch or breakfast.

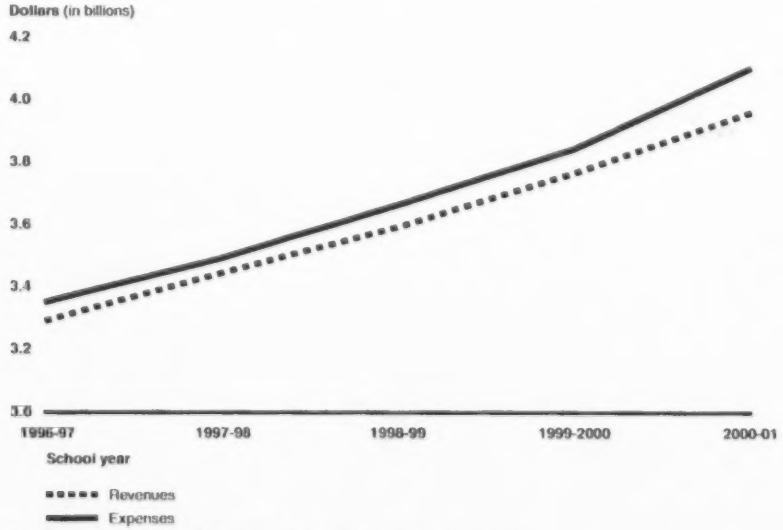
What GAO Found

Revenue from federal reimbursements and the sale of food were the principal sources of revenue for school food services in the six states GAO reviewed for school years 1996-97 through 2000-01. Federal reimbursements decreased slightly in proportion to the total, while revenues from food sales increased slightly. Funds from state governments and other sources represented a relatively small portion of total revenues and remained relatively stable as a share of total revenues.

Labor and food purchases were the principal expenses for the six states, sharing nearly equal proportions and changing only slightly. Labor expenses, which included salaries and benefits for food service employees, grew slightly while food expenses decreased slightly. Other expenses, such as contract services, made up a smaller portion of expenses, and this portion remained constant.

The six states had a small though increasing shortfall in total revenue compared to expenses over the 5-year period, as shown below. Their total expenses increased by about 22 percent, while their total revenues increased by about 20 percent. The portion of total school food service expenses covered by federal reimbursements declined from 54 to 51 percent, and the portion of expenses paid by state funds was small and declined slightly.

Changes in Total School Food Service Revenues and Expenses in Six States



Source: Florida, Missouri, New York, Ohio, Texas, and Virginia Departments of Education.

To limit their expenses and maximize their revenues, local school food authority officials reported buying food in bulk, hiring more part-time staff, expanding a la carte food sales and catering programs, and other strategies.

www.gao.gov/cgi-bin/getrpt?GAO-03-569.

To view the full report, including the scope and methodology, click on the link above. For more information, contact David D. Bellis at (415) 904-2272.

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Abbreviations

SFA	school food authority
USDA	U.S. Department of Agriculture

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United States General Accounting Office
Washington, DC 20548

May 9, 2003

The Honorable Tom Harkin
Ranking Minority Member
Committee on Agriculture,
Nutrition, and Forestry
United States Senate

The Honorable Tom Daschle
The Honorable Tim Johnson
The Honorable Jay Rockefeller
United States Senate

The National School Lunch and the School Breakfast Programs provide millions of children with nutritious meals each school day. The U.S. Department of Agriculture's (USDA) Food and Nutrition Service provides states with federal cash reimbursements for each meal served that meets federal requirements.[1] USDA also provides states with donated commodities for each school lunch served. Any child at a participating school may purchase these meals, and children from certain low-income households may receive the meals free or at a reduced price. A comprehensive study conducted a decade ago concluded that the combined federal reimbursements paid to states for the free breakfasts and lunches that students received covered the expenses of producing them.[2] However, the study was conducted before USDA established more stringent requirements for the nutritional content of school meals, beginning in school year 1996-97. The effect of these revised requirements on school food service finances is not known. Meanwhile, a recent rise in

[1]School lunches, for example, must meet the applicable recommendations of the Dietary Guidelines for Americans, which recommend that no more than 30 percent of an individual's calories come from fat and less than 10 percent from saturated fat. Regulations also establish a standard for school lunches to provide one-third of the Recommended Dietary Allowances of protein, Vitamin A, Vitamin C, iron, calcium, and calories. When schools serve meals that do not comply with federal nutrition requirements, program regulations allow the states to withhold federal reimbursements if the schools have not been acting in good faith to meet the requirements. However, USDA officials questioned whether holding back federal reimbursements offers a practical or realistic solution because of the possibility of program cutbacks or closure and the effect on the students, especially those receiving free or reduced price lunches.

[2]Abt. Associates, Inc., *School Lunch and Breakfast Cost Study - Final Report*, a special report prepared at the request of USDA, Oct. 1994.

the percentage of children who are overweight or obese underscores the importance of these programs, since they are designed to provide children with nutritionally balanced meals and to help them develop healthy eating habits.[3]

To participate in these programs, states provide a partial match to the federal reimbursements. They usually fund and operate the programs through their departments of education, which in turn have agreements with school food authorities (SFA). SFAs are local offices that are responsible for the administration of school food services in one or more schools. In addition to receiving federal cash reimbursements and state funds, SFAs may also receive funds from student and adult food sales and other sources, such as catering services, interest on deposits, and revenues from the sale of used equipment.

In view of the revised nutritional requirements, you asked us to study school food service revenues and expenses since the requirements went into effect. The objective of this report is to provide detailed information from school years 1996-97 through 2000-01 on the (1) sources of revenues available for providing school meals and how they have changed; (2) school food service expenses of producing meals and how they have changed; (3) school food service revenues, and particularly federal reimbursements, compared to the expenses of producing meals over this period; and (4) approaches that SFAs have adopted to manage their school food service finances. We are also issuing two other school meal related reports, one addresses the safety of the school meals and the other covers the efforts to serve nutritious meals and promote healthy eating in schools.[4]

To address each of these objectives, we collected and analyzed school year 1996-97 through 2000-01 revenue and expense data as reported to state agencies by all public school SFAs located in six states: Florida, Missouri, New York, Ohio, Texas, and Virginia. We selected these states

[3]The percentage of children ages 6 to 11 who are overweight has more than doubled, from about 7 percent in 1980 to about 14 percent in 1999, and the incidence of Type II diabetes—closely associated with obesity—has increased from 4 to 20 percent over the last decade.

[4]U.S. General Accounting Office, *School Meal Programs: Few Instances of Foodborne Outbreaks Reported, but Opportunities Exist to Enhance Outbreak Data and Food Safety Practices*, GAO–03-530 (Washington, D.C.: May 9, 2003) and *School Lunch Program: Efforts Needed to Improve Nutrition and Encourage Healthy Eating*, GAO-03-506 (Washington, D.C.: May 9, 2003).

because, of those states able to provide us with the needed data, they had the highest school meal programs reimbursement amounts in six of the Food and Nutrition Service's seven regions.[5] As a group, the six states received about 30 percent of the total federal school lunch and breakfast reimbursement funds dispersed nationwide in fiscal year 2001. In addition, we interviewed each of the six states' school food service directors, and 12 local SFA directors (2 in each state), to obtain information on approaches they took to manage their school food service finances in light of their overall revenue and expense picture.[6] We did not verify the information collected for this study. However, we reviewed the data we collected for reasonableness and followed up where appropriate. Moreover, the data we collected provided information on SFA revenues and expenses but did not permit us to calculate the cost of producing a reimbursable meal. A more detailed description of our study methodology is provided in appendix I. The results of the financial data in our study are reported in nominal dollars that can be generalized only for those states included in our review. We conducted our work between October 2002 and March 2003 in accordance with generally accepted government auditing standards.

Results in Brief

The principal sources of revenue for school food services in the six states combined for school years 1996-97 through 2000-01 were federal reimbursements and food sales; their proportionate share changed slightly over the 5-year period, with federal revenues decreasing from 55 to 53 percent of total revenues and food sales increasing from 38 to 39 percent of total revenues. Specific to food sales, revenue from a la carte foods, which are food items sold separately from the school meal programs and therefore not eligible for federal reimbursement, increased from about 40 percent of total food sales to about 43 percent over the period. Funds from state governments and other sources represented a relatively small portion of total revenues. Combined, total revenues grew from about $3.4 billion to about $4 billion in the six states over the period. While federal reimbursements and sales were consistently the largest revenue sources in

[5]We also requested the same data from California, the state in the seventh Food and Nutrition Service region with the highest school meal reimbursement amount; however, state officials were not able to provide us with the needed data. USDA does not require these data, and not all states collect them.

[6]We were also able to interview the California state director and 2 local SFA directors, and we include their responses in objective 4.

each of the six states, their share of total revenues varied considerably by state.

Labor and food purchases were the principal expenses in the six states combined, sharing nearly equal proportions and changing slightly over the period. Labor expenses, which include salaries and benefits for food service employees, grew from about 43 percent of total expenses to 44 percent. Food, which includes the value of USDA-donated commodities as well as purchased food, decreased from about 42 to 41 percent of total expenses during the period. Other expenses, such as contract services and capital expenditures, remained constant at about 15 percent of total expenditures. Combined, total school food service expenses increased from about $3.4 billion to about $4.1 billion over the period. While labor and food represented the principal expenses of school food services across the six states, their share of total expenses varied somewhat by state. There were greater variations among the states, however, in the proportion of their labor expenses made up of salaries and benefits. For example, in New York salaries and benefits ranged from about 90 and 10 percent respectively, while in Florida they ranged from about 74 and 26 percent respectively.

The six states' SFAs had a small though increasing shortfall in their total revenues compared to expenses over the 5-year period. Their total expenditures increased by about 22 percent, while their total revenues increased by about 20 percent. Although the federal reimbursements are adjusted annually for inflation, the portion of total school food service expenses they covered declined from 54 to 51 percent. The portion of total expenses covered by state funds declined by less than 1 percentage point to less than 3 percent. At the same time, the portion of expenses paid by other sources of revenue increased slightly, and the portion of expenses paid by revenues from school food service sales remained essentially unchanged over the period. We cannot determine the reason for the decline in the portion of total expenses covered by federal reimbursements because of data limitations. However, the decline in the portion of total expenses covered by state funds is likely a result of the federal method of calculating the state matching contributions, which are based on school year 1980-81 data and are not adjusted for inflation. Finally, the percentage of total expenses covered by federal reimbursements varied by state.

Local SFA officials reported adopting a variety of measures to both limit expenses and enhance revenues in order to manage their school food service finances. To contain expenses, they focused primarily on food and

labor costs. To reduce food costs, for example, they purchased food in bulk, found new ways to shop for lower-priced foods, and planned menus around USDA-donated commodities. To contain labor costs, they reduced staff numbers, replaced full-time staff with part-time staff, and served more pre-packaged foods that required less preparation. To increase revenues, they reported efforts to encourage more students to purchase their meals at school, such as increasing the number of food choices and enhancing the atmosphere of the school cafeteria. Officials also reported expanding their a la carte sales and catering. Raising school meal prices, another option for increasing revenues, was viewed as a last resort by most officials. Despite these strategies, many SFAs experienced year-end shortfalls, which were covered by their school districts' general revenue funds. However, some SFA officials expressed concern that their districts are also facing tighter budgets and may not be able to absorb the shortfalls in the future.

Background

The National School Lunch Act and the Child Nutrition Act of 1966 authorized the school lunch and school breakfast programs, respectively.[7] These school meal programs provide federal cash reimbursements to help states pay for nutritious lunches and breakfasts for children in participating public and private schools and residential child care institutions. The federal per meal cash reimbursement is adjusted annually for inflation.[8] Administered by the USDA's Food and Nutrition Service, the school meal programs are usually operated by state departments of education that have agreements with about 20,000 SFAs to provide the meals. SFAs that choose to take part in the school meal programs receive a federal cash reimbursement for each qualifying school lunch and breakfast they serve to children. SFAs participating in the school lunch program may also receive a federal reimbursement for snacks served to children participating in supervised after school educational or enrichment activities. These school meal programs are available in the 50

[7]The National School Lunch Act, as amended (42 U.S.C. 1751-1769), and the Child Nutrition Act of 1966, as amended (42 U.S.C. 1773).

[8]School lunch and breakfast reimbursement rates are adjusted annually by law to reflect the programs' operating expenses as indicated by the change in the series for food away from home of the Consumer Price Index for all Urban Consumers, published by the Bureau of Labor Statistics of the U.S. Department of Labor.

states and the District of Columbia, Guam, Puerto Rico, and the Virgin Islands.[9]

The amount that SFAs may charge for their school meals depends on the family income of participating children.[10] SFAs may charge for school meals according to the following categories:

- *Full price meals.* Children from families with incomes above 185 percent of the poverty level pay the meal price set by their SFA. There are no set limits on the amount that schools may charge students for a full price meal; however, participating SFAs must agree to operate a nonprofit school food service.

- *Reduced price meals.* Children from families with incomes between 130 percent and 185 percent of the poverty level may not be charged more than 40 cents for lunch and 30 cents for breakfast.

- *Free meals.* Children from families with incomes at or below 130 percent of the poverty level receive their meals free.

To receive federal reimbursement, SFAs must process an individual household application for most participants in the free and reduced price programs,[11] verify eligibility for at least a sample of households that apply, and keep daily track of school meals provided by eligibility category.

The levels of federal reimbursement per meal also vary according to the three categories. According to USDA, the per meal federal cash reimbursement is intended to cover the average expense of producing a school meal nationwide. The reimbursement rates shown in table 1 are the minimum amounts reimbursed to the contiguous states. Alaska and Hawaii receive higher reimbursement rates. Higher reimbursement rates are also

[9]The programs are also available to the children of armed forces personnel who attend schools overseas operated by the U.S. Department of Defense.

[10]After school snack reimbursements are provided to SFAs on the same basis as the income eligibility categories for school meals.

[11]In some cases, SFAs are not required to process an application. For example, children from households that participate in the Food Stamp Program, Temporary Assistance for Needy Families, or Food Distribution Program on Indian Reservations, are categorically eligible to receive free school meals and their families may not have to complete an application.

established for SFAs in certain low-income areas and districts identified by states as having critical needs.

Appendix II provides a more detailed listing of the school meal programs reimbursement rates and how they varied for school years 1996-97 through 2002-03.

Table 1: Minimum School Meal Programs Reimbursement Rates, School Year 2002-03

	Minimum reimbursement rates		
Reimbursement category	**Lunch**	**Breakfast**	**Snack**
Full price	$0.20	$0.22	$0.05
Reduced price	1.74	0.87	0.29
Free	2.14	1.17	0.58

Source: USDA.

SFAs also receive revenues from states for their school meal programs. As a requirement of participation, states must provide annual revenues for their school lunch program operations.[12] SFAs may also generate revenues by offering fee-based catering services and selling a la carte foods, which are food items that are sold separately from the school meal programs and therefore not eligible for federal reimbursement, as other methods of increasing their school food service revenues. Finally, SFAs may receive other cash revenues, such as the interest on deposits, and revenues from the sale of used equipment. In addition to cash reimbursements, SFAs may also receive donated commodity foods[13] from USDA, valued in school year 2002-03 at 15.5 cents for each lunch served in the previous school year.

[12]42 U.S.C. 1756 requires, generally, that states annually provide revenues for the operation of the School Lunch Program of not less than 30 percent of a portion of the federal reimbursements they received for the school year beginning July 1, 1980.

[13]One of the 50 states receives cash in lieu of USDA commodities. Schools may also receive "bonus" commodities, as they are available from surplus agricultural stock.

Federal Reimbursements and Food Sales Were the Principal Sources of Revenue over the Period, with Slight Changes in Their Proportionate Share of the Total

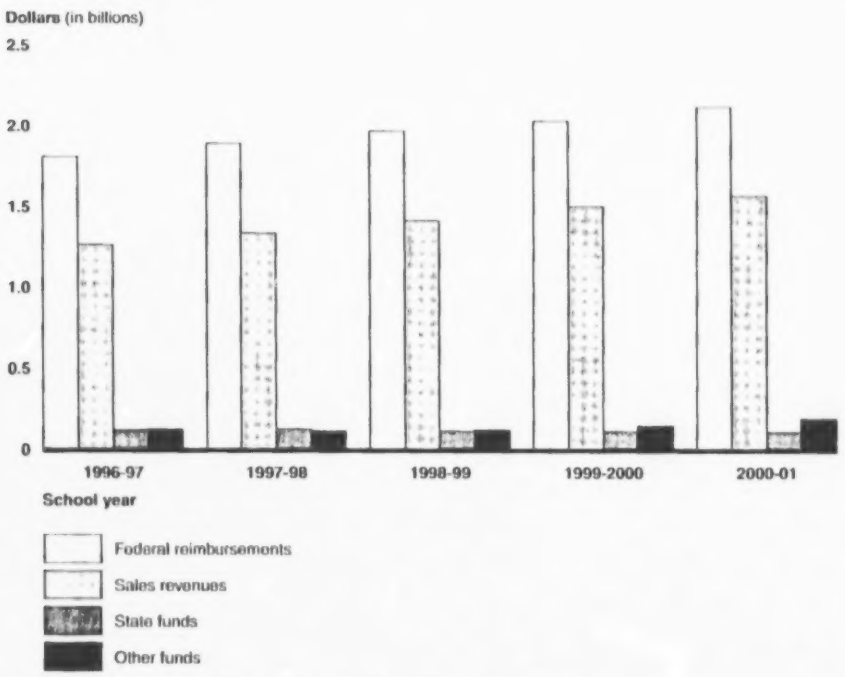
Federal reimbursements and sales revenues, which include student and adult meal payments, were the largest sources of school food service revenues in the six states during school years 1996-97 through 2000-01, with the share of federal reimbursements declining slightly and sales revenues increasing slightly. Funds from state governments and other sources represented a small portion of total revenues during this period. Specific to sales revenues, student payments for a la carte sales increased as a percentage of total school food service sales revenue. Finally, although federal reimbursements and revenues from sales were consistently the most significant revenue sources in each of the six states, their share of total revenues varied considerably by state.

School Food Service Revenues Come Primarily from Two Sources

Total school food service revenues reported by the six states increased from about $3.3 billion in school year 1996-97 to almost $4 billion in school year 2000-01. Federal reimbursements, including the value of donated USDA commodities, accounted for the largest share of revenues. Sales revenues, which include student and adult (e.g., schools administrators, teachers, and parents) payments, were the second largest source of revenues in these states. Revenues from state and local governments and other sources, which include catering services, interest on deposits, and the sale of used equipment, provided a relatively small portion of total revenues.[14] Figure 1 shows the various sources of revenues for school years 1996-97 through 2000-01.

[14]Available school meal program funds may also include unused program revenues, referred to as carryover, from prior school years, and unreported contributions from local governments, individuals, and other sources.

Figure 1: Sources of Revenues for School Food Services in Six States, School Years 1996-97 through 2000-01

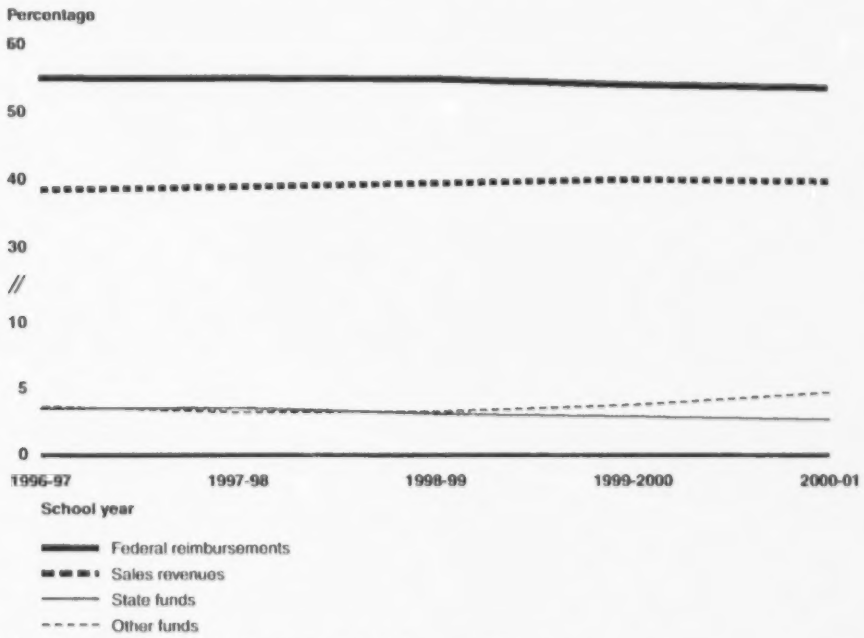


Source: Florida, Missouri, New York, Ohio, Texas, and Virginia Departments of Education.

Federal Revenues Declined Slightly in Relation to Total Revenues, While Sales Revenues Increased Slightly

As figure 2 shows, federal reimbursements declined modestly in proportion to total school food service revenues during school years 1996-97 through 2000-01. Federal reimbursements' share of total revenues decreased from about 55 to 53 percent. Conversely, during this period, revenues from food sales in relation to total revenues increased slightly from about 38 to 39 percent. Moreover, there was a less than 1 percentage point decrease in state funds to about 3 percent over this period and a 1 percentage point increase in other revenues to about 5 percent.

Figure 2: School Food Service Revenue Components as a Percentage of Total Revenues in Six States, School Years 1996-97 through 2000-01



Source: Florida, Missouri, New York, Ohio, Texas, and Virginia Departments of Education.

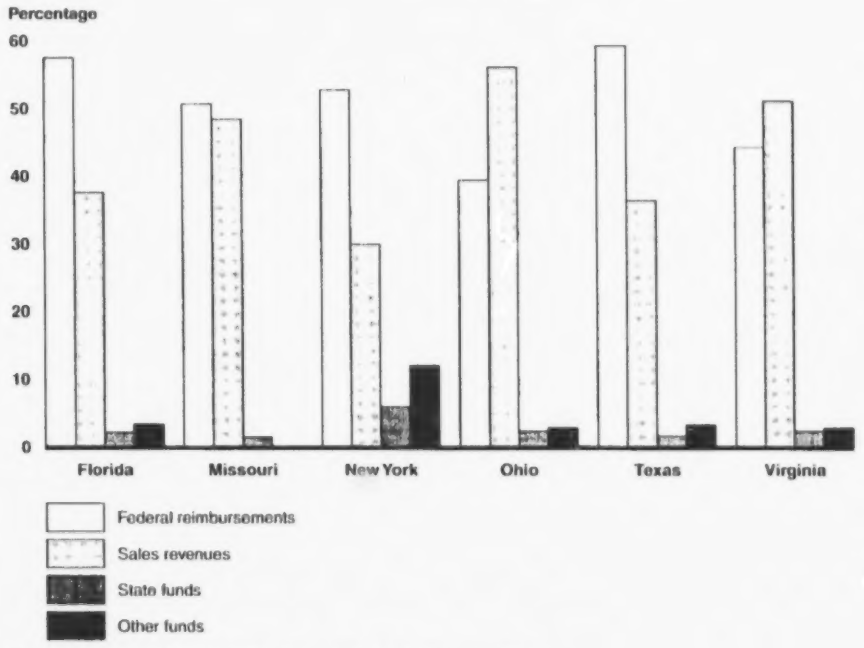
Specifically regarding revenue from food sales, information from five states that were able to separate the payments for a la carte foods from other meal sales showed an increase in a la carte revenues from about 40 percent of total sales revenues in school year 1996-97 to about 43 percent of total sales revenues in school year 2000-01. Because a la carte foods are not part of the school meal programs, they are not covered by the programs' nutritional requirements. As a result, some a la carte foods are nutritious, while others may have limited nutritional value.[15]

[15]For more information on the use of a la carte foods in schools and their implications for children's food choices, see GAO-03-506.

Share of Federal Reimbursements and Sales Revenues to Total Revenue Varied Considerably among the States

Although federal reimbursements and sales comprised the principal source of revenues for the school food services in each of the six states, their share of total revenues varied from state to state. As shown in figure 3, during school year 2000-01, federal reimbursements as a share of total revenue ranged from about 59 percent in Texas to about 39 percent in Ohio. A number of factors may be responsible for the variation in the share of federal reimbursements to total revenues reported across the six states. For example, a state may have a high proportion of low-income students that qualify for free or reduced price meals that receive a higher federal reimbursement rate, thereby increasing the relative share of its federal reimbursements. Another reason may be higher a la carte food sales that could increase the proportion of revenue from nonreimbursable food sales. Differences in the extent to which states utilize available USDA commodities may also account for some of the variation in federal reimbursements as a share of total revenues between states. However, because of data limitations, we cannot determine the reason for the variation. Sales revenues ranged from about 30 percent of total revenues in New York to about 56 percent in Ohio during the period. State revenues ranged from about 1 percent of total revenues in Missouri to about 6 percent in New York. Other revenues ranged from zero percent of total revenues in Missouri to almost 12 percent of total revenues in New York during the period.

Figure 3: School Food Service Revenue Components by State, School Year 2000-01



Source: Florida, Missouri, New York, Ohio, Texas, and Virginia Departments of Education.

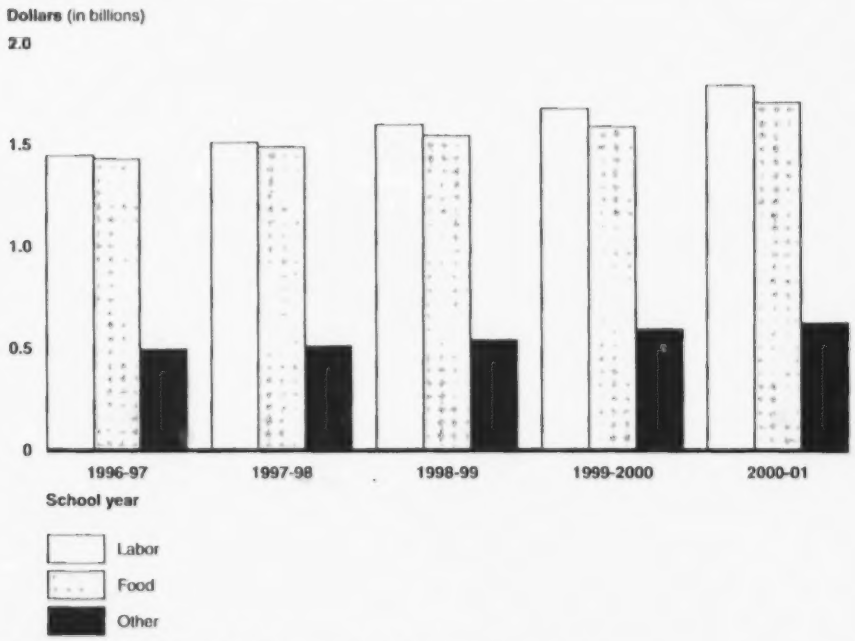
Labor and Food Were the Principal School Food Service Expenses over the 5-Year Period, with Slight Changes in Their Proportionate Share of the Total

Labor and food purchases accounted for most of the expenses of operating the school food services, with nearly equal shares of the expenditures and slight changes in their relative shares during school years 1996-97 through 2000-01. Other school food service expenses represented a smaller, but significant, portion of total expenditures. During this period, labor expenses slightly increased as a portion of total expenses, while food expenses slightly decreased. While labor and food were consistently the most significant expenses of operating the school food services in each of the six states, their share of total expenses varied somewhat by state.

Labor and Food Accounted for a Significant Portion of Expenses

Total school food service expenses reported by the six states have increased from about $3.4 billion to about $4.1 billion between school years 1996-97 and 2000-01. Labor and food purchases accounted for significant and nearly equal portions of the total expenses during the period. Labor expenses include the cost of salary and benefits of food service staff. Food expenses include the cost of purchased food and the value of USDA commodities used by schools in all food service activities. Finally, other school food service expenses, such as supplies, contract services, and capital expenditures, account for the remaining portion. Figure 4 shows the various expense components for school years 1996-97 through 2000-01.

Figure 4: School Food Service Expense Components in Six States, School Years 1996-97 through 2000-01

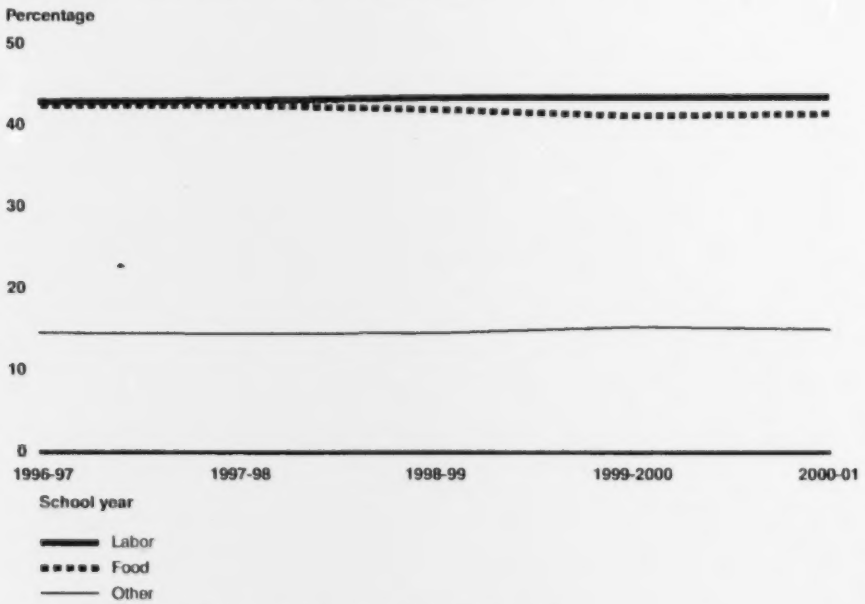


Source: Florida, Missouri, New York, Ohio, Texas, and Virginia Departments of Education.

Labor Expenses Increased Slightly in Proportion to Total Expenses, While Food Expenses Decreased Slightly

As shown in figure 5, as a percentage of total school food service expenses, labor costs increased slightly—from about 43 to about 44 percent—during school years 1996-97 through 2000-01. Food expenses as a percentage of total expenses modestly decreased—from about 42 to about 41 percent—during this period. Other expenses remained at about 15 percent of the total throughout the period.

Figure 5: Changes in Proportion of School Food Service Expense Components in Six States, School Years 1996-97 through 2000-01



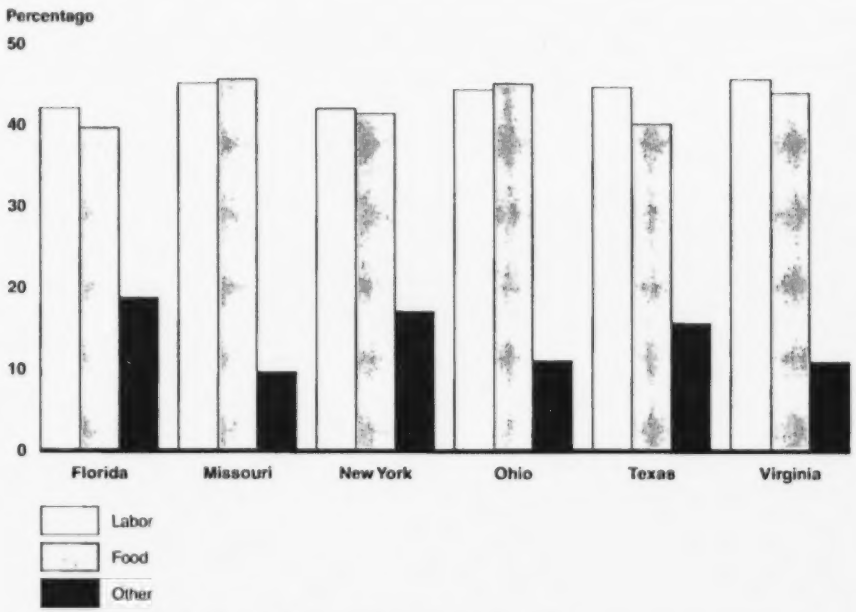
Source: Florida, Missouri, New York, Ohio, Texas, and Virginia Departments of Education.

Specifically regarding labor expenses, salaries and benefits changed less than 1 percentage point during this period, with salary expenses comprising about four-fifths of total labor expenses and benefit expenses comprising about one-fifth of the total across the states.

Share of School Food Service Expense Components to Total Expenses Varied Somewhat among the States

While labor and food represented the principal school food service expenses across the six states, their share of total expenses varied by state as shown in figure 6. Labor expenses ranged from about 45 percent of total expenses in Missouri, Texas, and Virginia to about 42 percent of total expenses in Florida and New York. Food expenses ranged from about 45 percent of total expenses in Missouri and Ohio to about 39 percent of total expenses in Florida in school year 2000-01. Other expenses ranged from 10 percent of total revenues in Missouri to about 19 percent of total revenues in Florida during that school year.

Figure 6: School Food Service Expense Components by State, School Year 2000-01



Source: Florida, Missouri, New York, Ohio, Texas, and Virginia Departments of Education.

Variations in the portion of labor expenses representing either benefits (e.g., health insurance and pensions) or salaries were more significant among the states. As a portion of total labor expenses, school year 2000-01 salaries ranged from about 90 percent in New York to 74 percent in Florida; conversely, benefits ranged from about 26 percent in Florida to 10 percent in New York. Over this period, the salary increases in two states—Florida and New York—grew more quickly relative to their benefit increases, whereas benefits grew more quickly than salaries in the other

four states. The salary increases in Florida and New York were responsible for the overall increase in salaries outpacing the overall increase in benefits across the six states.

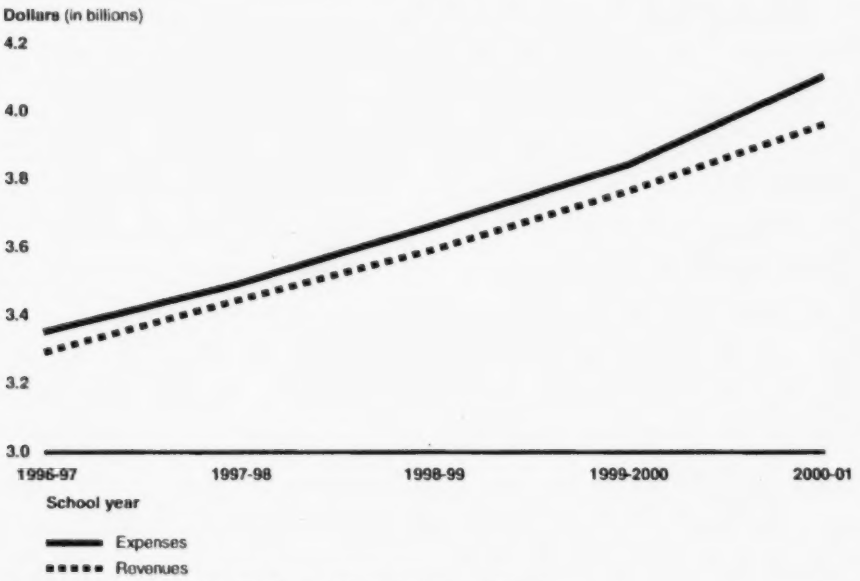
States Experienced a Small but Increasing Revenue Shortfall

Total school food service expenses were greater than total revenues in school years 1996-97 through 2000-01, and the gap between expenses and revenues grew slightly over this period for the six states combined. Moreover, federal reimbursements paid a smaller portion of school food service expenses during the period, as did state revenues. Conversely, the portion of expenses paid by other sources of revenues slightly increased, while the portion of expenses paid by revenues from school food service sales remained essentially unchanged during the period. Finally, federal reimbursements as a percentage of total expenses varied considerably by state.

School Food Service Expenses Have Slightly Outpaced Increases in Revenues

During school years 1996-97 through 2000-01, total SFA expenses increased from about $3.4 billion to about $4.1 billion, or about 22 percent across the six states, while total SFA revenues increased from about $3.3 billion to about $4.0 billion, or about 20 percent. As figure 7 indicates, the shortfall grew slightly over the 5-year period.

Figure 7: Changes in Total School Food Service Revenues and Expenses in Six States, School Years 1996-97 through 2000-01

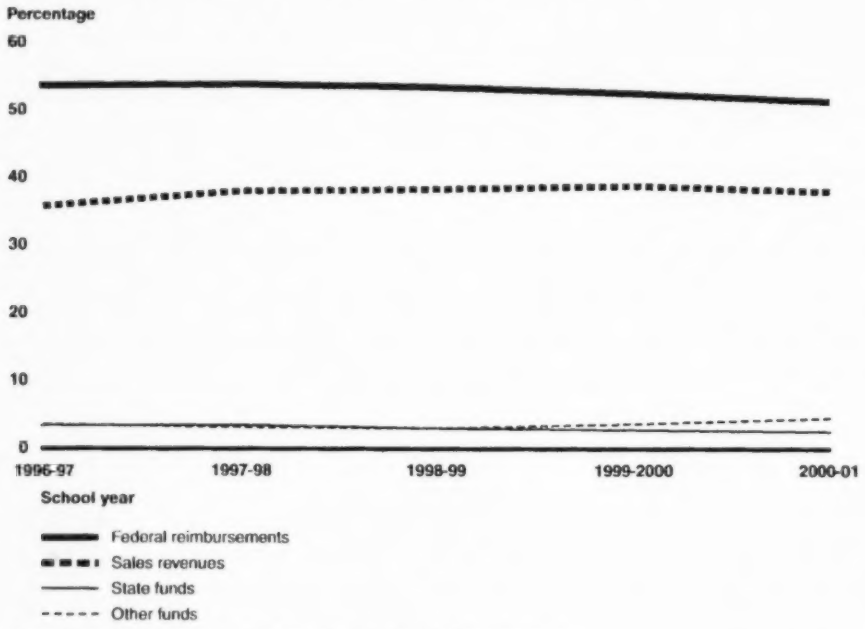


Source: Florida, Missouri, New York, Ohio, Texas, and Virginia Departments of Education.

Total School Food Service Expenses Covered by Federal Reimbursements and State Funds Have Declined

As figure 8 shows, the proportion of total school food service expenses paid by federal reimbursements and state funds declined slightly during school years 1996-97 through 2000-01 for the six states combined. Federal reimbursements paid a smaller portion of total expenses, declining from about 54 to 51 percent. The proportion of total expenses paid by state funds also declined by less than 1 percentage point to less than 3 percent during the same period. Conversely, the proportion of total expenses paid from other funds grew by about 1 percentage point to almost 5 percent, while revenues from meal sales as a proportion of total expenses were essentially unchanged at about 38 percent during the period.

Figure 8: Proportion of Total School Food Service Expenses Paid by Revenue Component in Six States, School Years 1996-97 through 2000-01



Source: Florida, Missouri, New York, Ohio, Texas, and Virginia Departments of Education.

The proportionate decline in federal reimbursement overall reflects the fact that total school food service expenses grew more quickly than federal reimbursement revenue. This may have occurred because the federal per meal reimbursement rate may not have risen as quickly as the cost per meal. However, without data on the average cost of reimbursable meals, we cannot determine if this is a reason for the decline. There are other possible reasons. For example, the growth in expenses may have exceeded the growth in federal reimbursement because schools are serving more a la carte foods, which could increase both expenses for nonreimbursable meals and revenue from nonreimbursable food sales, potentially decreasing the federal share. As another reason, a smaller proportion of students in an SFA may be eligible for or receiving free or reduced price school meals.

The decrease in the share of expenses paid by state revenues is the result of the federal funding requirement for states. To participate in the school lunch program, states must provide annual matching cash contributions

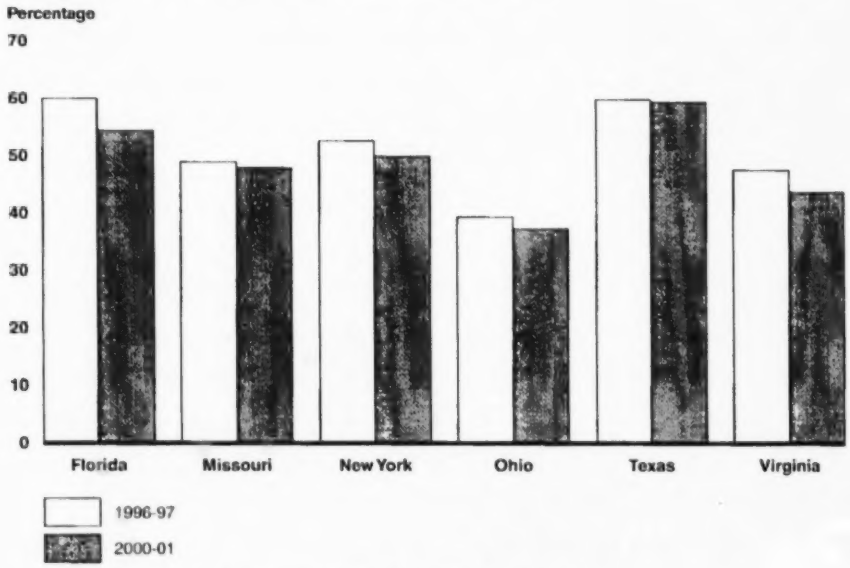
for program operations that equal 30 percent of the full price reimbursement for each eligible lunch they served in school year 1980-81.[16] Because each state's contribution is calculated on the fixed 1980-81 school year dollar amount, the contribution continues to decline each year as a share of the total school food service revenues and expenses.

Federal Reimbursements as a Percentage of Total Expenses Varied by State

The proportion of expenses covered by federal reimbursements varied among the six states. As figure 9 shows, during school year 2000-01, federal reimbursements covered about 37 percent of total expenses in Ohio and about 59 percent of total expenses in Texas. There are several potential explanations for this difference. For example, suppose that the sale of a la carte foods as a percentage of total revenues is higher in one state than another. This means that the proportion of expenses covered by a la carte revenues is also higher for that state, and therefore the proportion of expenses covered by federal reimbursements is lower. Further, improvements in a state's economic situation could result in fewer children eligible for free or reduced price meals. This change in eligibility category would result in schools receiving less federal reimbursement as a percentage of expenses. However, because of data limitations, we cannot determine specifically why the difference exists. Despite the variation among the states, the proportion of federal reimbursements as a percentage of total expenses was lower in school year 2000-01 than in school year 1996-97, ranging from less than 1 percentage point in Texas to about 6 percentage points in Florida.

[16]The required contribution is reduced to less than 30 percent if a state's average per capita personal income is lower than the national average. Of the six states, New York and Virginia had personal per capita incomes above the national average; Florida, Missouri, Ohio, and Texas had personal per capita incomes below the national average in 2001 (*Annual State Personal Income*, Bureau of Economic Analysis, U.S. Department of Commerce: Feb. 6, 2003).

Figure 9: Federal Reimbursements as a Percentage of Total School Food Service Expenses by State, School Years 1996-97 and 2000-01.



Source: Florida, Missouri, New York, Ohio, Texas, and Virginia Departments of Education.

States Used a Variety of Expense-Containment and Revenue-Producing Strategies to Manage School Food Service Finances

In an effort to minimize their revenue shortfalls, local SFAs employed two overall approaches to manage school food service finances—containing expenses and enhancing revenues. Efforts to contain school food service expenses focused primarily on food and labor—which comprised the largest share of all expenses. In order to contain these expenses, SFAs reduced expenditures, changed the way they purchased foods and the types of foods they purchased, reduced labor hours, and took steps to operate more efficient programs. SFAs further managed school food service finances by augmenting their food service revenues through increased sales from a la carte food items and catering; increased participation in the school meal programs; and in some cases, raising meal prices.

To Contain Expenses, Officials Focused on Food and Labor

Although fewer than half of the 14 local officials we interviewed said that their overall food expenses had increased in recent years because of USDA's revised school meal nutritional requirements, most of these officials said they saw the need to control food expenses. The approaches

used to contain food expenses varied by SFA. Many officials, for example, said they participated in food cooperative arrangements with other SFAs that allowed them to purchase bulk food items at lower cost. Some small SFAs reported that this arrangement was particularly useful for them because it provided them with greater purchasing power than they would have individually. Other officials attended local food shows that allowed them to shop competitively for lower-priced food items. To offset the costs of buying fresh fruits and vegetables, one SFA located in a state that participates in a "farm-to-school" pilot program with the USDA, obtained this produce from small farmers at low cost.[17] Taking another approach, one SFA reduced the number of school menu offerings and purchased fewer fresh fruits and vegetables for the school meal programs. Other officials planned their school meal menus around the donated food commodities from the USDA, which reduced the amount of additional food that needed to be purchased.

SFAs attempted to contain labor expenses by reducing the amount of labor and sought ways to increase the efficiency of the staff. According to most state and local officials, certain aspects of labor expenses have been rising, particularly salary scales and benefits. However, both are usually determined at the school district level and are therefore beyond the control of the SFA. In addition, a few local officials noted that many food service employees who are a part of the "baby boom generation" have begun to retire, and SFAs have, in some cases, found it necessary to offer higher salaries and more benefits to replace them.

Many local officials reduced their overall labor expenses by modifying staff numbers and hours—factors over which they did have control. For example, many local officials did not replace food service staff that retired, and they also reduced the number of hours worked by existing food service staff. According to three state directors we interviewed, SFAs were replacing full-time staff with part-time staff in order to reduce salary and benefit expenses. In addition, 10 SFAs reduced labor hours, and therefore labor expenses, by altering the type of foods they purchased. Officials of these SFAs said they reduced labor expenses by purchasing more prepared or prepackaged food items—such as chicken nuggets and

[17]The Small Farms/School Meals Initiative is a partnership program among USDA's Food and Nutrition Service and Agricultural Marketing Service, and the Department of Defense that encourages small farmers to sell fresh produce to schools and schools to buy this produce from small farmers. This is a cooperative program among federal, state, and local governments, as well as local farm and educational organizations.

frozen pizza—that required very little staff time to prepare. In addition, one SFA no longer offered sandwiches at lunch, because preparing them was too labor-intensive, and only provided fruits such as apples and bananas that did not need to be sliced. While some SFA officials noted that prepared food items tended to be more costly to purchase than "scratch" food items, many officials felt that these food cost increases were more than offset by the decrease in labor expenses.

In addition to reducing food and labor expenses, a small number of SFAs reported that they reduced overall school food service expenses by delaying or eliminating expensive kitchen equipment purchases. For example, when a dishwasher broke down in one SFA, officials there opted to use paper plates and plastic utensils rather than purchase a new machine.

A few SFA officials said that they undertook a variety of additional strategies that improved efficiency. In fact, five state directors told us that SFAs must operate meal programs as business-like operations with special focus on cutting costs wherever possible. One state agency reported that it sponsored seminars on increasing staff productivity and controlling costs for local directors. In another state, officials reported that an electronic point-of-sale system for the payment of food purchases improved staff productivity by increasing the number of students each staff member can serve by shortening the amount of time needed to pay for each meal.[18] A few SFAs sought to reduce costs by consolidating food production and storage to a few sites. In addition, some SFAs increased the use of self-serve meal lines to reduce the number of staff needed in the cafeteria. In one local SFA, the director reduced the number of staff breaks as a way to increase staff efficiency. In another SFA, staff reduced food waste by monitoring food items discarded by students and eliminating those items from the school menu.

To Enhance Revenues, SFAs Promoted the School Meal Programs and Also Increased a la Carte Sales

SFAs employed a variety of strategies to increase the amount of revenues available for their school food services. Almost all of the 14 SFAs we spoke with enhanced revenues for their food services by encouraging all students to purchase meals at school rather than bring lunch from home or buy it off campus. SFAs engaged in various activities to promote

[18]This state's electronic point-of-sale system used a credit-card-like device to conduct a cashless payment transaction.

participation, including increasing food choices for the reimbursable school meal programs, enhancing the atmosphere of the eating environment, and seeking input from students on food options. For example, 1 SFA offered students their choice of 10 different entrée options each day, while a national study has shown that most schools offer students 3 or fewer entrée options each day.[19] At another SFA, students were surveyed regarding which food items they preferred in the school cafeteria. Using yet another strategy, 1 SFA sought to increase the participation of students eligible for free or reduced price lunches by sending letters home to parents notifying them that although their children were approved to receive these meals, they were not participating.

For many SFAs, a la carte food items generated additional revenues for their school food services that allowed them to make ends meet financially. According to five state directors, a la carte sales have become an increasingly important source of revenue for SFAs. Unlike reimbursable school meals, a la carte food items are generally not subject to USDA's nutritional requirements.[20] A la carte offerings vary greatly by SFA—from snack and dessert items such as ice cream and potato chips in some SFAs to lunch items such as pizzas, hamburgers, and chicken nuggets in others. Some officials noted that a la carte programs might actually reduce participation in the reimbursable school meal programs, by drawing students away from a reimbursable school lunch. Moreover, a couple of officials noted that the growth in a la carte programs might be "at odds" with the goal of providing a nutritious meal to students.

Catering for school functions such as banquets and teacher training days was another important source of revenue for a few SFAs. Some SFAs also provided catering services to private schools, senior citizens, and others. For example, 1 SFA catered lunch a few days a week for a nearby senior citizen center as a way to raise additional revenue.

While a small number of officials we interviewed indicated that increasing the price of a full price meal was a viable option for increasing revenue for

[19]U.S. Department of Agriculture, Food and Nutrition Service, *School Nutrition Dietary Assessment Study-II Final Report*, Report No. CN-01-SNDAIIFR (Alexandria, VA: 2001). According to this study, 68 percent of all schools offered students 3 or fewer different entrée options for lunch each day.

[20]School meal regulations prohibit the sale of foods of minimum nutritional value, which includes carbonated beverages, certain candies, chewing gum, and water ices, in the school cafeteria during meal periods.

the school food services, most officials viewed raising the meal price as a last resort. Although the local director can in most cases request or recommend a meal price increase to the local school board or superintendent, some state and local officials indicated that such proposals were likely to be met with resistance from board members and parents. In addition, officials noted that increases in meal prices often resulted, at least initially, in fewer students purchasing a school meal.

Revenue Shortfall Sometimes Covered by Carryover Funds and Local Revenues

Many state and local SFA officials noted that, despite using strategies to enhance revenues and contain school food service expenses, SFAs often have difficulty breaking even financially in a given school year. SFAs sometimes maintain a limited fund balance containing excess money carried over from year to year for the school food service, and this funding can be used to cover a revenue shortfall in a given year. However, when SFAs were unable to cover their school food service expenses, many officials told us that local school districts, using general revenue funds, normally covered any shortage of funds. Since local school districts are facing tighter budgets than in years past, many officials noted that it was unclear whether school districts would continue to provide funding for school food services if they had a revenue shortfall. In fact, several state officials told us that school food service-related expenses that were previously paid by local school districts were being transferred to SFAs. Although the costs of these services—such as trash removal, pest control, linen services, and utilities—were attributable to the school food services, school districts had provided these services at no cost to the SFAs in better financial times.

Conclusions

According to our data, SFA revenues have not kept pace with expenses during school years 1996-97 through 2000-01; however, the extent of the shortfall could be considered modest to date. To cope with these shortfalls and to minimize the gap between revenues and expenses, some options are within the control of SFAs, while others are not. On the revenue side, federal law establishes the per meal reimbursement rates, the minimum state contribution, and the maximum rates SFAs can charge for reduced price meals. Options available to SFAs include increasing the number of students who obtain their meals at the school, expanding a la carte and catering sales, and increasing charges for full price meals. However, SFAs sometimes face resistance from parents and local officials to meal price increases. On the expense side, because SFAs usually do not set the salaries and benefits of food service personnel, available options to reduce their labor expenses include limiting the hours of their employees, cutting

the number of employees, altering the types and costs of foods they purchase for the programs, and enhancing other efficiencies related to labor and food expenses.

All of the SFA officials we spoke with had implemented some combination of these options, and without such measures the gap between revenue and expenses would likely have been greater. It is not clear from our work whether or not the SFAs could take additional measures to improve efficiency and further close the gap. Nor is it clear whether the gap will remain, decrease, or continue to grow. Nevertheless, the strategies SFAs have chosen for limiting expenses and enhancing revenues can have varying effects on achieving the goal of the school meal programs to ensure that the nation's youth consume nutritional and affordable meals while they are in school. Serving reimbursable meals that are more appealing to the student population could well encourage more students to eat a nutritious meal. On the other hand, relying more heavily on proceeds from the sale of a la carte items, which are not covered by the school meal programs' nutritional standards, could undermine that goal or at least offer less assurance that students are eating balanced meals. Such choices can, therefore, have critical consequences, especially given the current health and nutritional trends among the nation's children.

Agency Comments and Our Evaluation

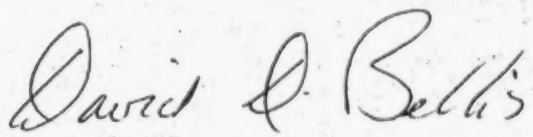
We requested comments on a draft of this report from the Secretary of Agriculture or her designee. On April 21, 2003, officials from the Department's Food and Nutrition Service, Child Nutrition Division, and Office of Analysis and Nutrition Evaluation, and the Department's Economic Research Service, provided us with the following oral comments on the draft. The officials said they were in general agreement with the findings as presented in the report. However, they said that recipients of our report should be aware that the report does not identify the cost of preparing a reimbursable school meal. They also noted that there are many factors that can contribute to the revenue and cost differences that we found between states, such as school meal program participation levels, changes in the household income of students, and the extent to which states use donated USDA commodities.

In addition, the officials provided data on the proportion of free, reduced price, and full price meals served for 4 of the 5 years in our study. The number of full price lunches served increased modestly in proportion to the number of free and reduced price lunches in five of our six states. This change may help explain the slight decline in federal reimbursement relative to other revenues and the declining share of total food service

expenses covered by federal reimbursements. However, without additional information, such as the increase in the number of a la carte foods sold, we are unable to determine the extent to which these changes in school meal participation played a role in the declining share of federal reimbursement. Finally, in addition to these observations, USDA provided technical comments that we have incorporated as appropriate.

We are sending copies of this report to the Secretary of USDA, appropriate congressional committees, and other interested parties. In addition, the report will be available at no charge on the GAO Web site at http://www.gao.gov.

If you or your staff have questions concerning this report, please call me on (415) 904-2272 or Kay E. Brown on (202) 512-3674. Key contact and staff acknowledgments are listed in appendix III.



David D. Bellis
Director, Education, Workforce,
and Income Security Issues

Appendix I: Scope and Methodology

This appendix discusses in more detail the scope and methodology for developing the revenue and expense information presented and for identifying the actions taken by school food authority (SFA) officials to manage their school food service finances. The scope of our review included the National School Lunch Program and the School Breakfast Program as they relate to public SFAs in selected states.

From the Food and Nutrition Service we obtained nationwide school meal programs information, including the (1) applicable federal reimbursement rates, (2) student participation, (3) number of school meals and snacks served, (4) cash reimbursements, and (5) commodity values.

To obtain statewide data on the revenues available to SFAs for providing school food services and the expenses of operating school food services, we selected seven states—one state from each of the Food and Nutrition Service's seven regions. We selected states that (1) were able to provide both school food service revenue and expense information for all of their SFAs and (2) received the highest amount of federal reimbursements in their respective region during fiscal year 2001. Five of the seven states selected—California, Florida, Missouri, New York, and Texas—received the largest federal cash reimbursements in their respective regions during fiscal year 2001. The two remaining states, Ohio and Virginia, received the second and third largest amount of federal reimbursements to the states in their respective regions.

We requested that each state provide annual school food service expense and revenue data as reported to state agencies by all of the public SFAs for school years 1994-95 through 2001-02, or for the years that were available during the period. We requested information on the (1) total annual amounts of revenues provided by federal, state, and other sources, and the value of USDA donated commodities and (2) expenses associated with producing school meals, including food service staff salaries and benefits, and food purchases. Six of the seven states were able to provide the requested data for school years 1996-97 through 2000-01. We were unable to obtain sufficient data to report on school years 1994-95 and 1995-96. In addition, during the course of our study, California notified us that it was unable to provide all of the data needed. For this reason, the revenue and expense information contained in this report does not include California.

We did not verify the data collected for this study. However, we reviewed the data for reasonableness and requested additional information when appropriate. First, we compared annual totals of certain data fields from year to year. If there were unusual jumps in these totals from year to year,

we asked the responsible agency to offer an explanation. Second, for the states that provided SFA-level data, we compared the number of SFAs in the data with the number of SFAs reported by the responsible agency. Third, we examined the relationship of data elements to identify any illogical associations. Fourth, we conducted interviews related to data reliability with the state food service directors. In our interviews with the responsible agency, we presented graphs that were created using the data provided us. We asked why certain patterns occurred in the graphs. Finally, in addition to the steps that we took to assess the reliability of the data, federal regulations require that each SFA participating in the school meal programs be routinely reviewed to determine its compliance with performance and regulatory standards. As a part of these reviews, SFAs must meet minimum reporting and record-keeping requirements. Reviews are generally conducted by appropriate state agencies and include evaluation of financial reporting systems.

To the extent possible, we excluded from our analyses other federal child nutrition programs, private schools, and residential child care institutions, which also participate in the school meals programs. While we collected only public SFA information for our study, the Missouri expense and revenue information includes both public and private SFA data because they were not tracked separately; however, the dollar amounts attributed to private schools are relatively small. Also, SFAs without full information for school years 1996-97 through 2000-01 were excluded from the analysis.

To identify actions taken by SFA officials to manage their school food service finances, we conducted phone interviews with the appropriate manager at each of the seven state agencies administering the school meals programs and with two local SFA managers within each state. We selected SFAs that both (1) experienced expenses that were larger than revenues during the past few years and (2) had large increases in expenses related to either food or labor.[1] We gathered information from these managers on the sources and amounts of funds available for school food service operations, the cost of producing meals, and what approaches SFAs were using to manage their food service finances. We also obtained their insights regarding revenue and expense changes and their

[1]Since the available data from California and Missouri did not allow us to identify the local SFAs that met our criteria, the state managers for the meal programs provided us with the names of SFAs they felt met our criteria.

observations regarding how these changes may have affected the school food services that they manage.

The results of the financial data described in our study are not generalizable beyond the six states that provided the required data. In addition, we cannot determine whether the changes we identified are statistically significant because we do not know the standard errors of our estimates. We conducted our work between October 2002 and March 2003 in accordance with generally accepted government auditing standards.

Appendix II: Federal School Meal Cash Reimbursement Rates, School Years 1996-97 through 2002-03

		Lunch		Breakfast		
School year	Meal type	Less than 60% of lunches served free or at reduced price	60% or more of lunches served free or at reduced price	Nonsevere need	Severe need	Snacks
1996-97						
	Full price	$0.1775	$0.1975	$0.1975	$0.1975	$0.0450
	Reduced price	1.4375	1.4575	0.7175	0.9125	0.2525
	Free	1.8375	1.8575	1.0175	1.2125	0.5050
1997-98						
	Full price	0.1800	0.2000	0.2000	0.2000	0.0400
	Reduced price	1.4900	1.5100	0.7450	0.9450	0.2600
	Free	1.8900	1.9100	1.0450	1.2450	0.5175
1998-99						
	Full price	0.1800	0.2000	0.2000	0.2000	0.0400
	Reduced price	1.5425	1.5625	0.7725	0.9775	0.2675
	Free	1.9425	1.9625	1.0725	1.2775	0.5325
1999-2000						
	Full price	0.19	0.21	0.21	0.21	0.05
	Reduced price	1.58	1.60	0.79	1.00	0.27
	Free	1.98	2.00	1.09	1.30	0.54
2000-01						
	Full price	0.19	0.21	0.21	0.21	0.05
	Reduced price	1.62	1.64	0.82	1.03	0.27
	Free	2.02	2.04	1.12	1.33	0.55
2001-02						
	Full price	0.20	0.22	0.21	0.21	0.05
	Reduced price	1.69	1.71	0.85	1.07	0.28
	Free	2.09	2.11	1.15	1.37	0.57
2002-03						
	Full price	0.20	0.22	0.22	0.22	0.05
	Reduced price	1.74	1.76	0.87	1.10	0.29
	Free	2.14	2.16	1.17	1.40	0.58

Source: Federal Registers and USDA.

Note: Higher reimbursements are provided to SFAs in which 60 percent or more of the lunches were served at a free or reduced price. Higher breakfast reimbursement rates are established for "severe need" SFAs in which 40 percent or more of the lunches were served free or at a reduced price and the nonsevere need rate is insufficient to cover the costs of the breakfast program. USDA provides higher school meal and snack reimbursement amounts in Alaska and Hawaii.

Appendix III: GAO Contact and Staff Acknowledgments

GAO Contact

Kay E. Brown (202) 512-3674 (Brownke@gao.gov)

Staff Acknowledgments

In addition to the individual named above, Peter M. Bramble, Jr., Cynthia G. Decker, and Michelle C. Verbrugge made key contributions to this report.

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